<u>SHELTER VICTORIA</u>

Summary of <u>Common Equity Co-operatives - a draft strategy for their Implementation in Victoria</u> (Revised Edition)

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The proposed Community Housing Expansion Program[§] (CHEP) funds could be used to fund a new type of Co-op - common equity rental co-ops (CERG's) in addition to other programs aimed at developing a community-based, non-profit housing sector. In a common equity rental co-op, the houses are owned on a group basis, rather than leased as is the case with the current Victorian Rental Co-ops. Membership shares remain nominal in value, making this form of housing easily accessible to those on low incomes. It is planned that the leasing co-op program would continue, however. Co-ops are particularly well-suited to the use of CHEP funds as their legal structure both ensures democratic control and enables them to borrow on the private market.

1. Concepts

The proposal is based largely on the Canadian model. Since 1973, 900 Co-ops have been established, housing 33,000 people.

It is proposed to use CHEP funds to subsidise finance borrowed through the private sector. Co-ops will be funded if they can attract private sector finance and where "there is a high level of tenant involvement in the management of a group's housing".

<u>Features of the proposed Co-ops</u>

* capital raised by a Government appointed Community Housing Trust (CHT) through letting out capital indexed bonds.

* on-lending packages would be in the form of capital indexed loans, with a small charge to cover administration costs. Low start capital indexed loans minimise initial subsidy needed.

* subsidies would be available in percent to number of Ministry of Housing eligible co-op members.

* subsidies would come out of CHEP funds. A CHEP State Co-ordinating Committee would be responsible for funding, setting guidelines, assessment and monitoring would be done by this body in conjunction with the CHT.

§ Subsumed under the Local Community Housing program in the 1984 Federal budget - total allocation $7m, total to Victoria $1.86m.

Features of the proposed Co-ops (cont)

* resourcing groups will help co-op groups :

  . prepare submissions
  . train members in management skills
  . carry out specialist functions eg: purchasing, architectural services

  It is hoped to fund two resourcing co-ops in the initial years.

* the proposed co-ops would have no worker or office, be small-scale between 7 and 20 households, have a social mix. It is hoped to set up five co-ops by 1985 with a range of income mixes.

A mix of low income tenants on rebated rents with those on higher incomes paying low end market rents would contribute to the financial viability.

Benefits of rental co-ops for moderate income earners - no deposit needed, don't have to tie up a greater percent of personal capital in purchase and maintenance of a house and provides an alternative to private rental which provides control, security of tenure, supportive networks and lower rents.

2. Overseas Models

(1) Top down approach

In Sweden, the prime movers are 2 large-scale, national co-op associations which provide a full-range of technical, administration and financial services. At a regional level, the societies plan and build co-op housing and develop management systems. When housing is completed the society forms the co-op to manage the housing. Prospective tenants first become involved only at this final stage. These co-ops are large in size and sacrifice tenant input in favour of economies of scale. Many of the co-ops contain an equity element - ie: members have tomake a substantial ingoing contribution.

(2) Member-initiated

The drive comes from community or tenant groups whose prime interest is gaining control over their own housing.

2. Overseas Models (cont)

(3) Objectives

General

* creation of an alternative housing strategy to home ownership which offers independence and control over housing without the associated high costs so as it is accessible to those on lower incomes.

* utilising private sector finance and community resources so as to provide a broader base for the spread of rental co-operatives.

* devolution of ownership of rental housing to community-based groups within a democratically accountable framework.

* provision of a management model which is flexible innovative, diverse and capable of responding to local and special interest needs eg: disabled

* increasing tenant satisfaction within a structure which while providing appropriate housing is both cost efficient and can demonstrate operating efficiency.

* providing for a social mix of income groups.

Specific Victorian Ministry of Housing Objectives

* targetting subsidies so they reach those groups perceived ; most in need.

* ensuring a degree of equity between this form of non-profit, rental housing and Ministry public housing.

* optimising scarce funding resources.

* adding to the stock of non-profit, rental housing through gaining access to private sector finance.

Specific Rental Housing Co-operative Objectives

* maximising authority and freedom from bureaucratic intervention.

* ensuring a degree of tenant member involvement and education.

* application of co-operative principles, as opposed to hierarchical and competitive principles.

* effective, efficient and democratic management of localised housing.

4. Raising Finance

The Co-op movement has mushroomed where governments have adjusted the financing system to ensure that capital is readily available from the private finance sector.

The Canadian system provides a government interest subsidy reducing the interest rate on loans borrowed on the private market down to 2%. Co-ops can borrow 100% of capital needed as the Federal Housing Authority guarantees each loan by insuring it for 100% of the capital cost. 95% of loans are raised through the national organisation controlled by representatives from credit co-operatives. The banking facility for this money is the peak credit co-op association.

The subsidy involved is both extensive and long-lasting in the case of each co-operative.

It is suggested that the major problem is not so much the high interest rate attached to private sector borrowing but the structuring of the loans themselves.

It is proposed to shift, in the initial years, from the use of traditional, credit foncier loans to low start, capital indexed loans.

Proposal to issue capital indexed bonds

It is recommended that funds be raised through the issuing of specific capital indexed bonds.

An investor would benefit in the following ways :-

These bonds would provide security against inflation - they would be indexed half-yearly to the Consumer Prince Index. Secondly, a half-yearly dividend yield would be obtained based on a set interest rate (3% is suggested) applied to their indexed compounding investment. The bonds would have a government guarantee, and would be exempt from tax if not redeemed within 10 years.

Taken together the index rate and real interest rate provide an average return of 16% to an investor. Bonds should be available to small investors - ie: bond coupon unit should be $100.

As it is intended to make loans run for a 35 year period a new bond series would need to be let every 10 years.

Other forms of fund-raising

Could raise traditional credit foncier loans through the banks and building societies. The South Australian Housing Trust has just borrowed from the Commonwealth Bank at 1% below home finance rate. This was a goodwill gesture and because of the rock solid government guarantee backing the loan.

4. Raising Finance (cont)

Other forms of fund raising (cont)

The N.S.W. Community Tenancy Scheme employed workers to negotiate at the local level the provision of land, capital, or to seek out joint development opportunities with churches, trade unions and local government.

It was felt that it would be unwise to raise capital through contributions by members because of difficulties created if these members leave.

It may be possible to establish this model of co-op, even if CHEP funds are not available, through the extension of the First Home Owner Scheme, through local government, through the use of CSHA funds or general community resources. To encourage donations, tax deductability could be sought for donations made to the Trust.

The Community Housing Trust (CHT)

The proposal to establish a government-appointed Board of Trustees via the State Ministry of Housing which contained, or could contract to obtain, the necessary financial expertise to :

. issue bonds and engage in other forms of fund raising;

. payout dividends and redeem bonds

. put together packages for on-lending to co-ops

. oversee the general administration of fund-raising and monitoring of funds let out eg: check submitting groups' financial viability.

It is recommended representatives from the following be selected/nominated:

- credit unions, rental co-ops or community housing groups, Ministry of Housing, C.H.E.P., State Co-ordinating Committee, banks of financial institutions, local government representative, (if local Government Housing Assistance Program funds are mixed with C.H.T. funds).

The Trustees would be paid, part-time positions. Expertise would be obtained through services of part-time advisors or by commissioning consultants. The C.H.T. should be placed within the Victorian Credit Co-operatives Association (VCCA) at arms length to the Ministry of Housing.

Banking Facility

It is hoped that the VCCA will be able to provide a central banking facility as recommended by the Financial Institutions Review Study.

4. Raising Finance (cont)

Administration

To cover administrative costs it is recommended that the rate between the real interest rate paid on bond dividends and the real interest rate paid on loans vary marginally. Alternatively interest on C.H.E.P. funds deposited in the central banking facility could cover the C.H.T.'s administrative costs.

Either the C.H.T. or the C.H.E.P. State Co-ordinating Committee (SCC) would have to make property development and financial assessments. (eg: checking out capacity to repay, value of house, plans for major renovations).

As mortgage holder, the CHT would have the power to direct the Registrar of Co-ops to put in an adminstrator and liquidate a co-op where default occurred.

Co-ops could borrow against their assets and get a second mortgage if they needed to refurbish their housing stock.

The CHT should hold a floating charge over all assets, so as the end of a co-op's loan period when property is debt free, the CHT would have the power to borrow against that Co-op's assets to set up further co-ops.

It is proposed that sitting tenants in the 36th year (when stock is debt free) should not reap the windfall profits of rents that only cover operating costs and not loan repayments. It would be inequitable to have sharply differing rents based on age of a co-op. It is proposed that there continue to be a charge payable to the Trust which would be used to strengthen the community housing sector. This could be related to the capital improved value of a co-op's Housing stock. The current minimum return expected by the State Government on its assets is 4%. This charge could even be used to reduce the cost rent in newer co-ops so as ceiling rents were the same for all CERC's.

5. Loan Structures

The proposal is based on minimising commitment of government funds and relating capacity to pay (which is expected to grow) to funds invested on a long-term basis.

Traditional credit foncier type loans are not suitable.

It is proposed co-ops borrow using a capital indexed loan structure. These loans would match the fund raising through capital indexed bonds except administrative costs would be added on.

The advantages of a capital indexed loan are compared with credit foncier loans. With a credit foncier loan repayments (providing interest rates do not change) remain constant over the life of the loan. This fails to take into account income growth. Repayments are high as a percentage of income in the first

5. Loan Structures (cont)

years, but the constancy of repayments in money terms means they rapidly lose their value in real terms in an inflationary environment. An example shows that in the first 5 years of a 25 year credit foncier loan 42% of all real interest and capital repayments are made and 67% are made in the first 10 years.

A capital indexed loan takes into account income growth. Income is assumed to rise at the same rate as inflation. and the loan is restructured accordingly. Such a loan structure allowed the co-op to jumb the high-cost hurdle imposed on starters in a credit foncier loan.

Capital Indexed Loans

Loan repayments have to match both bond redemption and the six monthly dividend yield to investors.

Repayments would have to be made every six months to cover the 3% real interest rate paid out as dividends on bond coupons, and would have to cover 1% administration costs of the Community Housing Trust.

As capital only has to be repaid by the Trust on redemption of the bonds every ten years, repayments of the principal by a co-operative are able to be invested by the Trust at a high interest rate until such time as bonds mature.

Setting the Ceiling Rate

Further work needs to be carried out to arrive at a formula for setting an appropriate cost rent for a particular co-operative where capital indexed laons are used. Alternatively, a cost rent set by State Housing Authorities as a result of rent averaging across all public housing could be used.

A "best case" model run was done to test a loan structure (see p.). The following assumptions had been made :

- Rent required is increased by 3% every six months to match assumed inflation rate of 6% per annum
- Operating costs per house per annum are a total of $1,300 (maintenance $100, provision for future maintenance $250, rates $700, insurance $50, administration $100, vacancies/ rent arrears $100)
- Loan period is thirty years
- Houses cost $65,000
- 2% resourcing fee allowed for

In this model it is assumed all tenant members are paying ceiling rent of $92 per week (or 85% of average Melbourne market rent).

Oops! mucked it up again. This is page 14. Please continue to page 8 and come back to this page later.

The objective is to establish a range of five co-ops commencing July 1985 (dependent, however on C.H.E.P. funding) These should have a range of income mixes.

. Survey existing leasing co-op membership to see if interested in forming core groups for C.E.R.C.'s

. Promote concept through community housing groups and generally

. Ask M.O.H. applicants to November 1984 seminar

. Bring out member of resourcing group in Canada for consulting and training

. Set up resourcing groups

. In conjunction with State Co-ordinating Committee develop guidelines on rent, membership profiles and minimal housing standards and monitoring procedures

. Develop maintenance manual

. Investigate setting up training course like that run by either Preston T.A.F.E. or by pilot resourcing group.

. Draft evaluation brief for pilot project

Resourcing Group

. Register by April 1985

. Selection by November 1984 by State Co-ord Committee

. Between April and July 1985 resourcing group would work up final plans with submitting groups

. Cost of setting up resourcing group $160,000 for salaries of full-time administrator, development officer and secretary and part-time builder/architect and accountant and administration.

12. Appendices

1. C.H.E.P. Draft Commonwealth Guidelines and Victorian Ministry of Housing comments

2. Indexed home lending - details of proposed scheme

3. Minimal Housing Standards drafted by C.H.A.S.

4. Ammendments to the Victorian Housing Act (1983) for rental housing co-operatives and Model rules for a rental housing

5. Loan Structures (cont)

Setting the Ceiling Rate (cont)

Other models were run with co-operatives having low-income members. These showed capital debts at the end of forty years.

It is believed that subsidies should be provided at the outset to contain total loan repayments within a thirty-five year period, otherwise the C.H.T.'s ability to redeem bonds could be seriously affected.

Subsidies should apply when there are low-income members. This would offset the internal cross-subsidisation of lower-income by higher-income members, at least to the equivalent to the First Home Owner Scheme. Such a deposit subsidy could be made available where a co-operative had a minimum of 25% Ministry-eligible members. A sliding scale is proposed. The higher the percentage of priority target groups in the co-operative, the greater the subsidy.

It is a matter of debate whether subsidies should be upfront capital grants, interest subsidies, or rent subsidies to individuals -- or some combination.

6. Funds Distribution

This would be the responsibility of a S.C.C. This should set priorities in relation to target groups, regions and project types and develop guidelines for assessment of submissions. This should be a broad-based Committee if it is to be effective in developing an alternative, non-profit housing sector. It would need access to either paid consultants or a team of specialists with property, financial, social planning and legal skills.

The role of these would be to:

. assess submissions

. approve purchases/renovations/construction

. draft contracts re: conditions of funding

. co-ordinate allocation of C.S.H.A. funds

. carry out research/policy development

In the short-term, the S.C.C. could be located in the State Housing Authority. In the long-term it would make sense to place this unit within the secretariat for the C.H.T.

7. Proposal model for the Common Equity Rental Co-ops (C.E.R.C.'s)

Membership Profile

Social mix and meeting housing needs of special groups (disabled, elderly, single parent families) are both important.

It is recommended that as a minimum a C.E.R.C. have 25% Ministry of Housing ineligible members. C.E.R.C.'s should not have to fit within priorities determined by the Accommodation Provision Programme but should be assessed in relation to community needs in general.

A submitting co-op would need to fix its total, proposed membership profile and contract with the S.C.C. that it would retain that profile even before the provision of a start-up grant to work up a plan with a resourcing group. Auditors would check the eligibility of tenants at entry point into a co-op as part of their annual report on the co-op's compliance with legislative requirements and funding guidelines. Alternatively, co-ops could agree to loan schedule revisions based on changes to its membership profile. This could be done at the time of the annual rent assessment with loan repayments going up or down, depending on whether or not there was a rise or fall in income. It would have the effect of either shortening or lengthening the loan period.

Rent

Rent should be determined on a cost rent basis, that is, based on the expected costs of a project.

Ceiling rents should not be allowed to exceed the prevailing market rent. A rental rebate formula has to be agreed upon (rebated rent would be between 20-25% of income).

If rebates were available to pick up the shortfall between an income-related rent and the ceiling rent, there would be no need to provide upfront capital subsidies through C.H.E.P. However, such an external rebate is not yet available. It is recommended that ceiling rents should not be allowed to exceed 75-85% of the market rent, so not to exploit middle-income earners. This would provide an incentive for these to join and would partly provide equity with middle-income home buyers.

Assessment Process

Co-ops would complete a skill training course and the design of their model at their own pace with help from a resourcing group paid through a start-up grant.

The sole concern of the S.C.C. would be whether a submitting group met with conditions of funding. Where subsidised funding could not keep pace with demand, approved submitting groups would need to go on a waiting list.

8. Resourcing Groups

Initially, at least one, possible two, resourcing groups would need to be established using C.H.E.P. funds.

Functions of a resourcing group would be:

- working up submissions

  (determine eligibility for subsidised funding and membership profiles, draft a detailed plan including creation of a management structure and estimating development costs per unit, undertake managment training in financial planning, maintenance, co-op principles, decision-making and meeting procedures)

- purchasing/renovation/construction options
- ongoing management training
- seeking co-op development opportunities
- research and information and development or manuals
- promotion
- financial advice
- maintenance
- monitoring
- legal advice

It is felt that to understand co-op principles and practice, resourcing groups should themselves be co-operatives. Three options exist:

- a Worker Co-op

  advantages

  - efficient in decision-making
  - minimal conflict
  - entrepreneurial because members' livelihood depends on this

  disadvantages

  - not accountable to primary co-ops
  - in the interests of survival it could identify too strongly with the wishes of the funding body
  - may protect incompetent workers

- a Secondary Co-op

  advantages

  - accountable
  - as a representative group it is better positioned to promote, lobby and encourage information exchange
  - check over-identification with funding bodies

8. Resourcing Groups (cont)

. a Secondary Co-op (cont)

disadvantages

-will revolve around existing co-ops rather than seek new
-development opportunities
-may be conflict between workers and consumers
-member co-ops may not have skills or vision to run a successful resourcing group

. Servicing Co-op (a mix of the above two types and can include representatives from the community in general)

potential conflict of interest between consumers, workers and community representatives.

It is proposed to set one or two resourcing groups in 1985. Others could be established a year later. The first resourcing group could be auspiced through the Collingwood, Richmond, Fitzroy Credit Co-op, C.H.A.S. and/or the Western Regional Housing Coucil. Resourcing groups could be set up on a regional basis. Another alternative is to call for submissions.

Groups would be licensed if they demonstrated:

. experience in co-operation, experience in community development training and management, organisational competance, access to range of consultants.

As registered co-ops, they would be subject to auditing and inspection by the Registrar of Co-ops.

A seeding grant of $160,000 should be available to the first group in the establishment year. Seeding grants would need to be available for a three to five year period. It is hoped that no ongoing grant wojld be necessary after this. Grants would, however, be available for specific research programs, eg. for various manuals.

These resourcing co-ops would work on a fee-for-service basis. Fees would be capitalised within the loan raised. Fees are estimated to range from 2% of capital costs for larger co-ops and 5% for small co-ops.

9. Housing

Under this model, the property development function is removed from the Ministry of Housing's direct control. Resource co-ops would assist. Housing standard guidelines should be minimal to allow maximum flexibility. Valuation could be done by registered private market valuers.

Area purchase price limits could be set by the S.C.C., but loan repayments should act as a constraint on purchase price limits. Some extras may be available such as funds for renovations for the disabled. Plans for renovations would have to be approved by the C.H.T. and/or the S.C.C.

9. Housing (cont)

It could be best to simply use Victorian Building Regulations as guidelines. A co-op should collectively set its own standards tailored to meet its own needs and then negotiate those with the S.C.C.

Basic training in maintenance skills should be mandatory for all co-op members.

Internal maintenance would primarily be the individual tenant's responsibility. It would be essential to establish a maintenance reserve and a program budget structure for all structural and syclical maintenance.

10. Legislative Framework

By and large, the existing Victorian Housing Act is adequate for establishing C.E.R.C.'s but it is recognised that reform of the Co-operation Act is necessary.

Compliance with co-op principles, adherence to a democratic framework and financial accountability would be monitored by Registrar of Co-ops.

The Victorian Credit Co-ops Association requires enabling legislation to act as a banking facility. Legislation would be required to establish the C.H.T.

Co-op leases would be subject to the provisions of the Residential Tenancies Act.

Provision would be made on winding up of a co-op that any property or assets remaining shal not be distributed to members but paid over to another co-op nominated by the co-or or used for the promotion of co-operation or any community benefit as determined by the co-op.

Co-ops would need to enter into a formal contract with the S.C.C. in relation to:

. development costs per unit and minimal housing standards

. retention of the membership profile

. an agreed ceiling, cost rent and internal rent subsidy for low-income earners.

. reporting back procedures and licensed auditors

11. Pilot Program

It is proposed that the M.O.H. set up a C.H.E.P. Interim Working Group which would liaise with the community groups and the Commonwealth.

Recommendations for action are as follows:

1. This report be extensively circulated seeking written comments.

2. Comments compiled, published and considered by the Working group.

3. Seminar held in November, 1984.

4. Comments sought from Canadian Co-op Housing Foundation and Canada Mortgage Housing Corporation.

Membership of the M.O.H. Working Group is to include:

. two representatives from Housing Services, two from Legal and Registry Division, one from Budget, Evaluation, Research Branch, Development and Property Division, one from management Services Division and one representative from the the Research and Review Unit. It can co-opt when necessary.

It should:

a) liaise re membership proposed and functions of State Co-ordinating Committee.

b) ensure its immediate establishment

c) consider the C.E.R.C. proposals

d) receive other proposals for use of C.H.E.P. monies

e) concsult where appropriate with Ministerial Advisory Committee on Co-operation, Department of Management and Budget (D.M.B.), the Financial Institutions Review Steering Committee (F.I.R.S.), the V.C.C.A. Shelter, C.H.A.S., Joint Co-ops and other groups.

It could consider the following tasks:

. talk to the Treasurer re: the issue of capital indexed bonds and their possible tax exemption

. talk to Hurford re: use of the First Home Ownership Scheme subsidies in C.E.R.C.'s

. release of C.H.E.P. funds to employ financial consultants

. liaise with D.M.B. about the impact of the bonds and gain government guarantee for them

. explore raising a bank or building society loan as stop-gap measure to begin a pilot project prior to introduction of bonds

. set up legal working group re: setting up C.H.T. so that a legally incorporated "broker" exists by August 1985.

. liaise with F.I.R.S. Committee re: recommendations enabling V.C.C.A. to become a central co-op bank.